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Legal Update

New Guidance for Irish Crypto AIFs

The Central Bank of Ireland (the "Central Bank") updated the guidance contained in its AIFMD Q&A document on April 4th, 2023, to revise its position in relation to certain AIFs obtaining exposure to crypto or digital assets. In summary the position relating to retail funds remains unchanged but there is now greater scope in relation to Qualifying Investor Alternative Investment Funds ("QIAIFs").

Background

The Central Bank has previously issued guidance on its view of Irish authorised funds containing exposure to digital assets. Digital Assets for these purposes are essentially defined to be private assets that depend primarily on cryptography and distributed ledger or similar technology and which are based on an intangible or non-traditional underlying. The prior guidance from the Central Bank has been the subject of prior Legal Updates available on our website but essentially provided that such exposure, either direct or indirect, will generally be viewed as inappropriate for UCITS or RIAIFs but may be considered acceptable for QIAIFs subject to certain limits of indirect exposure or if a submission is made that satisfactorily addresses key related regulatory concerns.

Updated Guidance for QIAIFs

The updated guidance issued by the Central Bank on 4 April 2023 was released through the new 47th edition of its AIFMD Q&A document. The relevant question is ID 1144 on whether a RIAIF or a QIAIF may invest either directly or indirectly in digital assets. The Central Bank will now permit a QIAIF to invest indirectly in digital assets subject to meeting the criteria below. However direct investment in digital assets will not be permitted until it is demonstrated to the Central Bank that a depositary meets the obligations under AIFMD to provide related custody or safe-keeping services.

Indirect Investment by QIAIFs

Where it is proposed that a QIAIF invest indirectly in digital assets the following requirements apply:
a) the prospectus must include clear disclosures regarding the nature of the proposed investment and the risks associated with investments in digital assets;

b) there must be an alignment between the redemption profile, the level of investment in digital assets and the likelihood of illiquidity (in normal and stressed conditions). Accordingly. where a QIAIF proposes to invest up to 20% of its net asset value in digital assets, the QIAIF may be structured as an open-ended fund provided that the portfolio as a whole is determined by the AIFM to be suitable for this structure, but where a QIAIF proposes to invest up to 50% of its net asset value in digital assets, the QIAIF must have either limited liquidity or be closed-ended.

In addition, the following requirements apply to its AIFM:

a) it must have an effective risk management policy to address all risks relevant to investment in digital assets. This must include, at a minimum, liquidity, credit, market, custody, operational, exchange risk, money laundering, legal, reputational and cyber risks;

b) it must carry out appropriate stress testing on the proposed investment in digital assets. This should reflect the asset price volatility of digital assets including the potential of complete loss;

c) it must have an effective liquidity management policy in place which includes a sufficient suite of tools to enable the AIFM to manage liquidity events arising in the QIAIF;

Retail Funds

In relation to retail investor alternative investment funds, or RIAIFs, the Central Bank still maintains the position that is highly unlikely to approve a RIAIF proposing any digital exposure.

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